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November 14, 2005

TO: Each Supervisor

FROM: Thomas L. Garthwaite, MD  
Director and Chief Medical Officer

A handwritten signature in black ink, which appears to read "Thomas L. Garthwaite". The signature is written in a cursive, flowing style.

**SUBJECT: DEPARTMENT OF HEALTH SERVICES FISCAL OUTLOOK**

This is to provide an update on the Department of Health Services' (DHS) fiscal outlook. As you know, the Department's Budget Committee of the Whole report was scheduled for discussion on the November 15, 2005 Board agenda. Due to a number of outstanding issues related to Medi-Cal Redesign, the proposed operating budget for the new LAC+USC Medical Center hospital, and the medical school affiliation agreements, all of which will impact the forecast, the Department will be asking that the Budget Committee of the Whole presentation be continued to the next set report on January 17, 2006.

It is the Department's expectation that greater clarity on the impact of these issues on the Department forecast shortfall, particularly in the initial years, will be available to include in the next fiscal outlook and thus will allow for a more informed discussion with your Board.

Although there are many uncertainties associated with the Department's ability to provide a current financial forecast, and while such a forecast represents only a snapshot in time, the following discussion and schedules do provide important insight into the Department's fiscal condition, particularly the impact of including Fiscal Year 2009-10 as part of the Department's financial planning cycle.

Current Fiscal Forecast

In the previous forecast, which went through Fiscal Year 2008-09, the Department's forecast cumulative shortfall was estimated to be \$889.1 million. As the County has closed the books on Fiscal Year 2004-05, DHS has updated its fiscal outlook by dropping this

year and adding Fiscal Year 2009-10. The schedule below provides a snapshot of the change in the Department's fiscal outlook from Fiscal Year 2008-09 and 2009-10.

	<u>\$ Estimates in Millions</u>	
	<u>Thru FY 08-09</u>	<u>Thru FY 09-10</u>
Year-End Cumulative <u>Fund Balance / (Shortfall)</u> as of September 2, 2005	\$(889.1)	\$(1,280.7)
Significant changes per Attachment A	<u>15.1</u>	<u>23.1</u>
New Year-End Cumulative <u>Fund Balance / (Shortfall)</u> as of October 25, 2005.	<u>\$(866.0)</u>	<u>\$(1,258.2)</u>
Forecast Annual Operating Shortfall	<u>\$(383.6)</u>	<u>\$(392.2)</u>

The line titled "New Year-End Cumulative Fund Balance/Shortfall" represents the cumulative fund balance shortfall for Fiscal Years 2006-07 through 2009-10. The line titled "Forecast Annual Operating Shortfall" represents the funding needed to continue the Department's existing programs in each respective fiscal year. Attachments A and B detail the changes in the Department's fiscal forecast.

The very slight improvement in the Fiscal Year 2008-09 forecast shortfall can be attributed to a number of changes in the assumptions related to revenue realization and expenses by both the Department and the Chief Administrative Office. Among the changes noted in Attachment I are savings of \$66.7 million in Fiscal Year 2009-10 from the transfer of ownership or closure of Rancho Los Amigos National Rehabilitation Center. A detailed explanation of these items is included in Attachment A.

As noted above, there are a number of potential changes, for which sufficient detail is not yet available, that are not included in this forecast, but will affect the Department's projected budget shortfall. These include the estimated operating costs for the LAC+USC replacement hospital beginning in Fiscal Year 2007-08, increases in funding for the medical school affiliation agreements, and replacement of Computerized Tomography (CT) scanners in DHS hospitals. Analysis of the fiscal impact of these items is continuing and will be discussed in the next forecast provided to your Board in January 2006.

The Department continues to work with the State Department of Health Services and the federal Centers for Medicare and Medicaid Services to resolve a number of outstanding issues technical issues with regard to the implementation of Medi-Cal Redesign, such as the definition of an allowable certified public expenditure. As indicated in the last Budget Committee of the Whole report, this and other yet to be

Each Supervisor  
November 14, 2005  
Page 3

determined factors could ultimately have a significant impact on the Medi-Cal Redesign estimates included in the Department's fiscal outlook.

Further, as the Department mentioned in its previous report, the Medi-Cal Redesign package enacted in October did not address the proposed expansion of mandatory Medi-Cal managed care to cover aged, blind, and disabled Medi-Cal recipients (now being referred programmatically as "seniors and persons with disabilities"). The State administration has begun to work on a proposal to mandate inclusion of this population into managed care, with the intent of beginning implementation with Los Angeles County in January 2007. These individuals represent 40 percent of the Department's Medi-Cal patients. Presently, only 14 percent of these individuals statewide are voluntarily enrolled in managed care, and the remainder are fee-for-service Medi-Cal. While still to be determined, the revenue implications of the potential shift of this patient population into managed care could be significant. The Department continues to work with the Chief Administrative Office and the Disproportionate Share Hospital (DSH) Task Force on these issues.

Please let me know if you have any questions.

TLG:ak

Attachments

c: Chief Administrative Officer  
County Counsel  
Executive Officer, Board of Supervisors

**COUNTY OF LOS ANGELES - DEPARTMENT OF HEALTH SERVICES**  
**SUMMARY OF CHANGES IN THE DHS FISCAL OUTLOOK**  
**SEPTEMBER 2, 2005 THROUGH OCTOBER 25, 2005**

	Fiscal Year / Columns / \$ In Millions					
	<u>05-06 / (1)</u>	<u>06-07 / (2)</u>	<u>07-08 / (3)</u>	<u>08-09 / (4)</u>	<u>09-10 / (5)</u>	<u>Total / (6)</u>
(1) Revised Estimated <u>Cumulative</u> Year-End Fund Balance / (Shortfall) - September 2, 2005	\$ 204.5	\$ (139.8)	\$ (497.5)	\$ (889.1)	\$ (1,280.7)	\$ (1,280.7)
(2) Adjust <u>FY 09-10 expense base</u> for salary COLA, employee benefits, services and supplies CPI, pharmaceutical CPI, debt service, and capital projects offset by adjustments to the <u>revenue base</u> for Medi-Cal fee-for-service, AB 915, CBRC, Medicare, Vehicle License Fees.	\$ -	\$ -	\$ -	\$ -	\$ (75.5)	\$ (75.5)
(3) Net savings from the <u>closure/transfer of Rancho</u> on June 30, 2009.	-	-	-	-	66.7	66.7
(4) Adjust <u>employee benefits</u> for the current fiscal year per estimates developed in October 2005 and restate Workers Compensation and Retirement estimates for FY's 06-07 and 09-10 based on updated information from the CAO.	6.7	(1.5)	(0.4)	6.9	6.9	18.6
(5) Adjust <u>Clinical Resource Management</u> costs for the current fiscal year per estimates received in October 2005.	18.3	-	-	-	-	18.3
(6) Increase <u>Interest expense</u> for the current fiscal year per estimates developed in October 2005 based on updated information from the Auditor-Controller.	(5.9)	-	-	-	-	(5.9)
(7) Extend the <u>Navigant Consulting, Inc.</u> agreement for six months from November 2005 through April 2006 for consulting services at K/DMC, as approved by the Board on October 25, 2005.	(5.7)	-	-	-	-	(5.7)
(8) Change in <u>FY 05-06 operating forecast</u> received in October 2005/ Other minor ongoing changes to the future years estimates.	0.4	0.8	2.4	1.1	1.3	6.0
(9) Forecast improvement/(reduction) roll-forward	-	13.8 <sup>(B)</sup>	13.1 <sup>(B)</sup>	15.1 <sup>(B)</sup>	23.1 <sup>(B)</sup>	-
(10) Revised Estimated <u>Cumulative</u> Year-End Fund Balance / (Shortfall) - October 25, 2005 <sup>(A)</sup>	<u>\$ 218.3</u>	<u>\$ (126.7)</u>	<u>\$ (482.4)</u>	<u>\$ (866.0)</u>	<u>\$ (1,258.2) <sup>(C)</sup></u>	<u>\$ (1,258.2)</u>

**Notes**

- (A) Does not include the impact of the medical school agreements which are currently being negotiated for LAC+USC, H/UCLA and OVMC. Assumes CBRC/FQHC will be extended for each year beyond FY 04-05. CBRC extension for LA County's outpatient and clinic care was included in the FY 05-06 Adopted State Budget. A Medi-Cal State Plan Amendment to extend the program is currently pending CMS approval.
- (B) These amounts represent the cumulative change in the forecast from the prior fiscal year. For example, the \$13.8 million in FY 06-07 is \$218.3 million - \$204.5 million from FY 05-06.
- (C) Includes additional Medi-Cal Redesign funding of \$119.1M in FY 09-10 over what would have been included without Medi-Cal Redesign. This increases the benefit of Medi-Cal Redesign from \$383.9M over four years, as reported last time, to \$503.0M over five years.

**COUNTY OF LOS ANGELES - DEPARTMENT OF HEALTH SERVICES**  
**DHS FISCAL OUTLOOK - OCTOBER 25, 2005**  
(\$ IN MILLIONS BASED ON FY 05-06 SUPPLEMENTAL BUDGET RESOLUTION)

Line #	FISCAL YEARS / COLUMNS								TOTAL / (8)
	2002-03 / (1)	2003-04 / (2)	2004-05 / (3)	2005-06 / (4)	2006-07 / (5)	2007-08 / (6)	2008-09 / (7)	2009-10 / (8)	
1. Surplus/Deficit as of June 28, 2002		\$ (328.8)	\$ (549.2)	\$ (709.4)					
2. Scenario III Reductions / Use of Designation Funds	*(see note)	287.8	327.8	357.5					
3. Original Fiscal Stabilization Revenue Request to help fund Scenario III (Not Budgetary Shortfall by FY)	*(see note)	\$ (58.8)	\$ (221.4)	\$ (351.9)	\$ (387.3) <sup>(A)</sup>	\$ (423.7) <sup>(A)</sup>	\$ (461.8) <sup>(A)</sup>	\$ (503.4) <sup>(A)</sup>	\$ (2,408.3)
4. Actual / Forecast Update <sup>(B) (C) (D) (E) (F)</sup>		283.9	340.0	321.8	789.2 <sup>(G)</sup>	136.1	157.9	162.9	(215.7)
5. Actual / Forecast Surplus/(Shortfall)	\$	283.9	\$ 281.2	\$ 100.4	\$ 447.3	\$ (251.2)	\$ (285.8)	\$ (298.9)	\$ (719.1)
6. Beginning Fiscal Year Fund Balance		121.0 <sup>(H)</sup>	353.1 <sup>(H)</sup>	452.8 <sup>(H)</sup>	19.7 <sup>(H)</sup>	467.0	215.8	(50.0)	-
7. Estimated Cumulative Year-End Fund Balance/(Shortfall)	\$	384.9	\$ 634.3	\$ 553.2	\$ 467.0	\$ 215.8	\$ (50.0)	\$ (348.9)	\$ (719.1)
8. Defer Rancho Closure/Divestiture per Harris/Rodde Settlement through FY 07-08 and for One-Year Post-Settlement.	\$	-	\$ (49.5)	\$ (53.9)	\$ (59.5)	\$ (69.4)	\$ (78.9)	\$ (81.8)	\$ -
9. Defer LAC+USC 100 Bed Reduction per Harris/Rodde Settlement through FY 09-10.	-	(16.1)	(29.8)	(31.9)	(34.1)	(36.5)	(39.1)	(41.8)	(229.3)
10. Net Impact of Harris/Rodde Proposal at LAC+USC <sup>(I)</sup>	-	-	-	(5.4)	(1.4)	8.7	19.2	19.8	40.9
11. Net Impact of Harris/Rodde Proposal at Rancho <sup>(J)</sup>	-	-	-	(0.4)	11.1	14.8	-	-	25.5
12. Net Impact of Operating Rancho for One-Year Post-Settlement <sup>(K)</sup>	-	-	-	-	-	-	17.0	-	17.0
13. Cost of Plaintiff Attorney Fees	-	-	-	(2.2)	-	-	-	-	(2.2)
14. Impact to Beginning Fiscal Year Fund Balance	-	-	(65.9)	(149.3)	(248.7)	(342.5)	(432.4)	(517.1)	N/A
15. Revised Estimated Cumulative Year-End Fund Balance/(Shortfall)	\$	384.9	\$ 568.7	\$ 403.9	\$ 218.3	\$ (126.7)	\$ (482.4) <sup>(L)</sup>	\$ (866.0) <sup>(L)</sup>	\$ (1,258.2) <sup>(L)</sup>
16. Use of Designation Funds - Decrease/(Increase)		\$ (183.8)	\$ 184.8	\$ 185.8	\$ 218.3	\$ -	\$ -	\$ -	

**NOTES TO FISCAL OUTLOOK**

- \* The \$58.8 million of FY 02-03 service cuts are efficiencies already in the FY 02-03 budget base at this point in time and; therefore, doesn't appear on this schedule.
- (A) These amounts are extrapolations from the original 90% Medicaid block grant request used to determine the fiscal stabilization revenues for the June 2002 DHS Strategic Plan, which only extended through FY 05-06.
- (B) Includes revenues previously shown separately (Measure B, SPCP/UPL Waiver, SB 855, and the Federal portion of the Outpatient Lawsuit Settlement).
- (C) These amounts are potentially improved by the managed care supplement proposal currently being worked on with the State and Federal governments.
- (D) Reflects an "unidentified budget surplus" of \$90.0M for FY's 05-06 through 09-10 added by the CAO.
- (E) Does not include the impact of the medical school agreements which are currently being negotiated for LAC+USC, H/UCLA and OVMC for FY's 05-06 through 09-10. Assumes CBRC/FQHC will be extended for each year beyond FY 04-05. CBRC extension for LA County's outpatient and clinic care was included in the FY 05-06 Adopted State Budget. A Medi-Cal State Plan Amendment to extend the program currently pending CMS approval.
- (F) Does not take into account the opening of the LAC+USC replacement facility in July 2007 for FY's 07-08 through 09-10. Per LAC+USC, current financial projections for the new LAC+USC are still in progress.
- (G) Reflects release of the \$96.1M trust fund reserve.
- (H) Reflects a beginning fund balance of \$368.9M less the \$245.9M fund balance included in the FY 02-03 Supplemental Budget Resolution.
- (I) Reflects a beginning fund balance of \$384.9M less the \$31.8M fund balance included in the FY 03-04 Supplemental Budget Resolution.
- (J) Reflects a beginning fund balance of \$568.7M less the \$115.9M fund balance included in the FY 04-05 Supplemental Budget Resolution.
- (K) Reflects a beginning fund balance of \$403.9M less the \$384.2M fund balance included in the FY 05-06 Supplemental Budget Resolution.
- (L) Per Harris/Rodde settlement proposal, census will be reduced through a reduced average patient length of stay (8.5 to 8.0); includes enablers and resulting savings.
- (M) Per Harris/Rodde settlement proposal, includes Rancho takeover negotiations, oversight panel and review with plaintiffs, liver clinic monitoring and reducing Rancho's budgeted census from 191 to 147.
- (N) Reflects savings from operating Rancho at a reduced census (147) for one-year post-settlement in preparation for closure/divestiture on June 30, 2009.
- (O) The forecast annual operating shortfalls for FY's 07-08, 08-09, and 09-10 are \$355.7M, \$383.6M, and \$392.2M, respectively.